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No. 89-1958

IN THE

Supreme Court of the United States

OCTOBER TERM, 1989

COLOWYO COAL COMPANY AND PEABODY COAL COMPANY,
Petitioners,

v.

MANUEL LUJAN, JR., SECRETARY OF THE UNITED STATES
DEPARTMENT OF THE INTERIOR,
Respondent.

**On Petition For A Writ Of Certiorari
To The United States Court of Appeals
For The District of Columbia**

BRIEF OF COLORADO-UTE ELECTRIC ASSOCIATION, CITY OF COLORADO SPRINGS, COLORADO AND CENTRAL POWER AND LIGHT COMPANY AS *AMICI CURIAE* IN SUPPORT OF PETITIONERS

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This *amici curiae* brief is submitted in support of the petition for a writ of certiorari. Petitioners and Respondent have consented to the filing of this brief. *Amici* appear on behalf of their electric customers and rate-payers.

INTEREST OF THE AMICI

Colorado-Ute Electric Association ("CUEA") is an electric generation and transmission cooperative cre-

ated pursuant to the Rural Electrification Act of 1936, as amended. 7 U.S.C. §§901-950 (1982). Through its 14 member distribution cooperatives, CUEA serves nearly 200,000 consumers (representing a population of approximately 600,000 persons) in primarily rural service areas covering parts or all of 49 of Colorado's 63 counties (representing almost two-thirds of the area of the State of Colorado). CUEA was organized in 1941, and began electric utility operations in 1959, so that its distribution cooperative members, who serve rural families and businesses, could obtain a reliable and economical source for their electric power needs. The City of Colorado Springs, Colorado ("Colorado Springs"), located in central Colorado, owns and manages a non-profit generation, transmission and distribution network serving residential and industrial customers in the Colorado Springs area. Central Power & Light Company ("CP&L"), a subsidiary of Central and South West Corporation, is a generation, transmission and distribution company serving a 44 county area in southern Texas with a population of approximately 1.25 million persons and containing over 200 cities and towns.

Coal mined by the Petitioners from federal leases is purchased by *Amici* pursuant to long-term purchase agreements.[1] These agreements contain royalty pass-

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[1] CUEA's long term purchase agreement with Colowyo is for approximately 1,500,000 tons of federal coal per year until 2017. CUEA will also purchase federal coal from Peabody in amounts averaging 700,000 tons per year until the year 2004. Colorado Springs will purchase approximately 550,000 tons per year from Colowyo until the year 2004. CP&L will purchase approximately 1,500,000 tons per year from Colowyo until the year 1994.

through provisions requiring that *Amici* reimburse Petitioners for federal coal royalties or any increases therein paid by Petitioners. At the time *Amici* executed their long-term purchase agreements, the federal coal royalty assessed on Petitioners' coal production, and passed-through to *Amici*, equalled 20 cents per ton. Petitioners' existing coal leases limited the power of the Secretary to raise royalties to reasonable adjustments necessary to reflect materially changed conditions. Despite these lease provisions, in the mid-1980's, the Secretary of the Department of the Interior, citing the provisions of the Federal Coal Leasing Amendments Act of 1976, Pub. L. No. 94-377, 90 Stat. 1083, readjusted Petitioners' federal coal leases and imposed the 12.5 percent *ad valorem* royalty rate applicable to new leases issued after 1976 on Petitioners' existing pre-1976 leases. Due to the pass-through nature of these increases, *Amici* now are liable for royalty costs of $3.30 to 3.65 per ton of coal. Over the life of their coal supply contracts, *Amici* calculate that this increase will cost their co-operative members and rate-paying customers a combined total of $240 million; nationally, *Amici* project a total royalty-based price increase for electric customers of approximately $2 billion over the next ten years. The annual increase in royalties imposed on CUEA exceeds the total margin (profit) earned by CUEA in any year of its existence. These huge increases are both unfair and unlawful.

The unfairness of Interior's actions is self-evident. In the 1970's, when *Amici* were preparing to expand generating capacity, elimination of dependency on foreign oil and natural gas and the increase in the use of coal was a top domestic priority of the Nixon, Ford

and Carter Administrations.[2] Congress responded by enacting a series of laws prohibiting utility use of certain fuels, such as natural gas, and directing utilities to use, or increase their use of, alternative fuels—primarily coal.[3] At tremendous expense, *Amici* and other utilities throughout the West, Midwest and Southwest built large coal-fired generating facilities. These large facilities required massive amounts of capital. CUEA spent over one billion dollars to build its mine-mouth coal-fired generating facilities at Craig Station Units 1,2 and 3 near Craig, Colorado which have a combined capacity of 1,200,000 kilowatts. These facilities were financed through the use of Ru-

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[2] *See, e.g., President Nixon's Energy Message to Congress*, (April 18, 1973), *Energy Mgmt.* (CCH) ¶ 504 at 506-507 (1973) ("I urge that highest national priority be given to expanded development and utilization of our coal resources." *Id.*); *President Ford's Energy Message to Congress* (February 26, 1976), *Energy Mgmt.* (CCH) ¶ 701 at 687 (March 9, 1976) ("Coal must be used increasingly as an alternative to scarce, expensive or insecure oil or natural gas supplies." *Id.*); *President Carter's Energy Address* (April 18, 1977) (The energy crisis "is unprecedented in our history;" America must declare the "moral equivalent of war" in response; and "[w]e can protect ourselves from uncertain supplies . . . by making the most of our abundant resources such as coal." *Id.*).

[3] *See, e.g., Emergency Petroleum Allocation Act of 1973*, Pub. L. No. 93-159, 87 Stat. 627 (1973); *Federal Non-nuclear Energy Research and Development Act of 1974*, Pub. L. No. 93-577, 88 Stat. 1878 (1974); *Energy Reorganization Act of 1974*, Pub. L. No. 93-438, 88 Stat. 1233 (1974); *Energy Supply and Environmental Coordination Act of 1974*, Pub. L. No. 93-319, 88 Stat. 246 (1974); *Energy Policy and Conservation Act*, Pub. L. No. 94-163, 89 Stat 871 (1975); *Energy Conservation and Production Act*, Pub. L. No. 94-385, 90 Stat. 1125 (1976); and *Powerplants and Industrial Fuel Use Act of 1978*, Pub. L. No. 95-620, 92 Stat. 3289 (1978).

ral Electrification Administration and National Rural Utilities Cooperative Finance Corporation loans and loan guarantees. CP&L spent over $250 million to build its 601,000 kilowatt facility at Coleto Creek, Texas. Colorado Springs spent over $110 million for the construction of its coal-fired facility near Fountain, Colorado. Given the costs of developing a western, low-sulfur coal strip mine, coal companies—such as Petitioners—could not obtain commercial financing until utilities—such as *Amici*—contractually agreed to purchase specified tonnages over long periods. Utilities such as *Amici*, in turn, expected reasonable certainty as to the future costs of the coal purchased, and certainly never anticipated that in addition to their multi-billion dollar investments in coal and coal facilities, the Federal Government would endeavor to extract billions of additional dollars by "readjusting" the federal coal royalty.

Amici have been injured by the Federal Government's unilateral decision to supercede existing lease terms. At the time *Amici* entered into their long-term coal supply contracts with Petitioners, the Secretary of the Department of the Interior had by regulation consistently construed his power to readjust coal lease terms as limited to fact-specific changes needed to meet "materially changed conditions." The Secretary has replaced the required regulatory analysis with the mechanistic imposition of a royalty rate totally divorced from any analysis of existing economic conditions. Had the Secretary examined economic conditions for western Colorado coal, he would have discovered the high cost associated with mining that coal,[4] the lack of alternative markets for that

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[4] Because Colorado's federal coal reserves are relatively costly

coal, the lack of alternative supplies for electric generating facilities, the fragile condition of the coal mining industry and the western Colorado economy and the financial conditions of *Amici* as principal purchasers of this coal. All of these factors demonstrate the complete irrationality of imposing a 12.5 percent royalty on existing leases.

ARGUMENT

CONGRESSIONAL EXERCISE OF SOVEREIGN POWER TO ABROGATE CONSIDERATION DUE UNDER A CONTRACT BETWEEN THE UNITED STATES AND PETITIONERS VIOLATES PRINCIPLES OF DUE PROCESS AND JUST COMPENSATION AND WRONGFULLY FRUSTRATES THE REASONABLE EXPECTATIONS OF *AMICI*

This case presents important issues regarding those principles that govern contracts with the Federal Government for the development of federal resources: Does the Secretary of the Interior or the Congress have the power to abrogate unilaterally the provisions of a federal coal lease and thus deprive the lessee and those in privity with the lessee of the reasonable business expectations contained in that lease? If the Secretary of the Interior or the Congress possesses that power, can it be exercised with impunity, unrestrained by principles of Due Process or Just Compensation?

The Court below held that Congress, in the exercise of its "sovereignty", could abrogate the compensation terms of a contract to which the United States was

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to mine, the *ad valorem* percentage royalty rate results in a much higher royalty than that for coal from areas with low mining costs, such as the Powder River Basin in Wyoming.

a party without implicating either Due Process or Just Compensation considerations and that, if any ambiguity existed in the coal lease contract, it must be resolved so that such power was preserved. D.C. Cir. Slip Opinion, reprinted at Petitioners App. A, 17a - 20a.[5] The Court of Appeals' reasoning leads to a legal paradox. On the one hand, in order to effect the royalty change proposed here, the Federal Government must resort to its power as sovereign. On the other hand, however, the Court of Appeals found that the Federal Government did not impinge Due Process or Just Compensation despite taking from the lessees a substantial value of their leases through exercise of that sovereignty.

In essence, the Court of Appeals gives the Federal Government all the benefits of sovereignty with none of the obligations or limitations. *Amici* are injured by the irresponsible exercise of this sort of sovereignty since they are contractually obligated to pay for any royalty increases[6] and are therefore the economic party in interest. The Petitioners' property right is comprised of the lease rights to extract and sell fed-

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[5] The Court of Appeals' suggestion that "if one who wishes to obtain a contractual right against the sovereign" that is immune from this sort of abrogation, then one "must make sure that the contract confers such a right in unmistakable terms." D.C. Cir. Slip Opinion, Petitioners App. A, 20a, is illusory. Federal coal leases are very much contacts of adhesion to which the prospective lessee can neither add nor subtract terms or conditions.

[6] When agreeing to this term and condition in their coal supply contract with Petitioners, *Amici* justifiably assumed that the royalty readjustments would be consistent with long-standing administrative precedent and would not create an uncompensated taking.

eral coal upon the payment of a fixed royalty. The Court of Appeals has held the Congress and the Secretary may take additional value from the Petitioners regardless of the terms and conditions of Petitioners' leases. Execution of the provision in the lease setting the amount to be paid for the lease rights is not an exercise of Congress' power as sovereign; rather it is Congress' exercise of its proprietary powers. Hence, *Merrion v. Jicarilla Apache Tribe*, 445 U.S. 130 (1982), concerning a Tribe's *taxing* power (an attribute of sovereignty) relied upon by the Court of Appeals to uphold the unilateral change in the royalty rate (*i.e.*, the consideration received under the contract), is inapposite.

A court must engage in a higher level of review where the Federal Government modifies its own contractual obligations. Rights against the United States arising out of a valid contract are protected under the Fifth Amendment and cannot be annulled unless pursuant to the "federal police power or some other paramount power." *Lynch v. United States*, 292 U.S. 571, 579 (1934). Further, "complete deference to a legislative assessment of reasonableness and necessity is not appropriate because the State's self-interest is at stake." *United States Trust Co. v. New Jersey*, 431 U.S. 1, 25-26 (1977). The Court of Appeals' construction of these federal coal leases allows Congress to exact greater compensation unilaterally. Moreover, the Court below in sanctioning the Federal Government's conduct in this matter, has wholly disregarded the reasonable expectations of *Amici* and Petitioners. At the time *Amici* decided to build their coal-fired plants, and to contract with Petitioners, the Government had established a settled policy of royalty rate adjustment

over a number of decades and with respect to hundreds of coal leases. *Amici* do not quarrel here with the government's right to specify a 12.5 percent royalty rate for *new* federal coal leases. Parties entering into such leases or purchasing the coal from them do so with fair warning of the economic facts of life. No such "fair warning" was given to *Amici*. *Amici*, and parties similarly situated, built reasonable expectations on the continued effect of federal policy regarding royalties found in pre-1976 coal leases.[7] The government's change in established policy unlawfully and substantially deprives Petitioners of their property interest in their leases and frustrates the reasonable business expectations of parties such as *Amici*. The Court of Appeals has effectively held that whenever the Federal Government grows dissatisfied with its bargain or the compensation received under a valid, long-term contract, it simply may unilaterally change the compensation, apparently to any amount it desires.[8] Not only does the Court of Appeals endorse this sort of Federal action, but it treats such conduct as a protected aspect of sovereignty, immune from Due Process or Just Compensation considerations. The Court erred by not imposing on the Federal Government the important procedural strictures guaranteed by the Fifth Amendment.

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[7] Again, *Amici* do not object to reasonable increases in coal royalties for materially changed conditions; for example, to keep pace with inflation. However, the increases of nearly 2000 percent in the federal royalties paid by *Amici* go far beyond the bounds of reasonableness.

[8] The Court's conclusion is at odds with its own precedent in *Fox v. Ickes*, 137 F.2d 30 (D.C. Cir. 1943), *cert. denied*, 320 U.S. 792 (1943) (Secretary enjoined from raising price for water received under existing reclamation contract).

We respectfully urge this Court to review the decision below, for the reasons set forth herein and those advanced by Petitioners, and to consider the important question of whether Congress may use its power as sovereign to amend contracts entered into pursuant to its proprietary powers without restraint of the Fifth Amendment.

CONCLUSION

This Court should grant Petitioners' request for a writ of certiorari to review the D.C. Circuit's decision.

Respectfully submitted,

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